VZCZCXRO8315
PP RUEHCN RUEHDE RUEHGH
DE RUEHHK #2600/01 1740737
ZNR UUUUU ZZH
P 230737Z JUN 06
FM AMCONSUL HONG KONG
TO RUEHC/SECSTATE WASHDC PRIORITY 7419
INFO RUEHGP/AMEMBASSY SINGAPORE PRIORITY 2965
RUEHAD/AMEMBASSY ABU DHABI 0086
RUEHBJ/AMEMBASSY BEIJING 8926
RUEHBY/AMEMBASSY CANBERRA 1666
RUEHLO/AMEMBASSY LONDON 0680
RUEHUL/AMEMBASSY SEOUL 2566
RUEHTC/AMEMBASSY THE HAGUE 2283
RUEHKO/AMEMBASSY TOKYO 4133
RUEHCN/AMCONSUL CHENGDU 0852
RUEHDE/AMCONSUL DUBAI 0033
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RUCPDOC/DEPT OF COMMERCE WASHDC
RHMFIUU/COGARD INTELCOORDCEN WASHINGTON DC

UNCLAS SECTION 01 OF 04 HONG KONG 002600

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STATE FOR EB/TRA AND EAP/CM
DHS/CPP FOR PIZZECK

E.O. 12958: N/A
TAGS: EWWT ETRD ENRG HK
SUBJECT: HONG KONG PORT'S COMPETITIVENESS AS A SEA-TRADE
LOGISTICS HUB

¶1. (U) Summary. In 2005, Hong Kong's port shipped more goods to the U.S. than any other, while Singapore overtook Hong Kong's position as the world's busiest container port. Pearl River Delta (PRD) ports collectively are much more significant than Singapore, but Hong Kong's share of the Pearl River Delta shipping market has been declining. This loss of market share is due to higher costs and longer distances from PRD's exporting factories to Hong Kong. Since they are also the major operators of PRD ports in the PRC, Hong Kong port operators have been indifferent to this market share loss. End summary.

Hong Kong Port's Competitive Difficulties

¶2. (U) In 2005, Hong Kong's port shipped more cargo to the U.S. than any other port in the world. It is an impressive facility, with some 80 international shipping lines providing over 400 container liner services per week, connecting to over 500 destinations worldwide.

¶3. (U) The logistics industry, the backbone of Hong Kong,s role as the "gateway to China," has always been expected to suffer as China opened up to the rest of the world. For the past several years, Hong Kong's logistics industry has been migrating across the border, just as the manufacturing industry has been doing over the past two decades. Dozens of Hong Kong-based logistics companies are also setting up on the mainland under the auspices of the Hong Kong-PRC free trade agreement, the Closer Economic Partnership Arrangement (CEPA). While Hong Kong firms are maintaining their control over the PRD logistics business, their move across the border has led to the replacement of Hong Kong jobs with mainland ones.

¶4. (U) In 2005, Hong Kong handled a record 22.43 million twenty-foot equivalent units (TEUs) of cargo, a 2.02 percent

increase from 2004. Growth in Hong Kong's port industry is slowing, while that in other PRD ports is rapidly growing. In 2004, the number of containers Hong Kong handled increased by a faster 7.3 percent. Neighboring Shenzhen handled 16.2 million TEUs in 2005, 18.6 percent more than 2004. Shanghai grew by 24.3 percent, totaling 18.08 million TEUs. Hong Kong's share was slightly less than 60 percent of all goods shipped out of the Pearl River Delta last year, but this market share is shrinking rapidly. In 2000, Hong Kong shipped 18 million TEUs, while Shenzhen handled 4 million, which gave Hong Kong an 82 percent share. Hong Kong had been specializing in the higher end of the market, owing to the territory's much more intensive use of technology and efficient handling of shipments. Shenzhen focused more on low-cost bulk exports. As exporters have grown used to shipping from mainland ports, however, they have begun using Shenzhen for more long-distance shipments to Europe and the United States, while using Hong Kong for more intra-Asia shipments.

¶5. (U) In addition to Shenzhen's three main ports at Yantian, Chiwan, and Shekou, Hong Kong also faces increasing competition from other PRD ports.
Guangzhou is upgrading its terminal facilities, while Hong Kong investors are developing new ports in Zhuhai (next to Macau) and Shenzhen. The HKG has responded by completing a feasibility study for a tenth container terminal on Lantau Island, for which it is now assessing the potential environmental impact. The HKG stresses that South China's trade will continue to grow, ensuring that Hong Kong Port's business will expand, albeit as a smaller share of a larger pie.

¶6. (U) Due in part to Hong Kong's need to share business with the rest of the PRD, Singapore overtook Hong Kong as the busiest port in the world last year. In 2006, Singapore processed 3.5 percent more containers than Hong Kong, totaling 23.2 million TEUs. Hong Kong had been the world's busiest container port in 13 of the 14 years prior to 2006. Singapore's large growth in container traffic reflects its importance as a transshipment hub, particularly in the growing Australian-European trade. By consolidating containers in Singapore, firms save on such shipments.

¶7. (SBU) While mainland Chinese ports are adding capacity and growing rapidly, they will not be able to absorb all the capacity that currently goes through HK for another decade. In the meantime, however, higher costs in Hong Kong are driving the Hong Kong port operators to shift more business to the mainland. HIT, Hong Kong's biggest port operator, which operates half of Kwai Chung's berths directly, sold 20 percent of its Hong Kong port operations to the Port of Singapore Authority (PSA) in June 2005. Five months later, it announced that it was taking a 65 percent stake in the third phase of Shenzhen's Yantian Port in exchange for an amount close to what it gained in the Kwai Chung sale. Hong Kong's second largest terminal operator, Modern Terminals, is investing USD 568 million to develop Shenzhen's new Dachan Bay Container Terminal, envisioned eventually to have 24 berths. In addition, Hong Kong's terminal operators are arguing against the HKG's plan to build Hong Kong's tenth container terminal in northern Lantau Island, claiming that demand does not exist for this facility. In contrast, port operators supported the construction of Hong Kong's ninth container terminal on Tsingyi Island, which broke ground in
¶2000.

¶8. (U) Hong Kong is losing market share primarily because it is cheaper to ship from the mainland. McKinsey estimates that it costs about USD 300 more to ship a forty foot container from Hong Kong than through Shenzhen ports. This cost differential is due to two factors: higher cross-border trucking costs and higher terminal handling charges (THC), which are fees charged by the shipping lines to shippers to

compensate them for costs entailed in their use of port facilities. Higher cross-border trucking costs represent two-thirds of the cost differential, or USD 200.

Terminal Handling Charges (THC) - A Private Sector Matter
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¶9. (SBU) The HKG cannot easily solve the THC differential. It has consistently said that THC is a private sector arrangement in which it will not interfere. Shipping lines charge shippers a uniform THC for the same port, the level of which is set at global shipping conferences. Although port operators in Hong Kong have lowered the fees they charge shipping lines for using their berths, the shipping lines have not passed on all these savings to the shippers. In addition, the Hong Kong port operators (most of whom also operate ports in Shenzhen) still charge more for the use of their Hong Kong facilities. A representative from one of the port operators told us that the higher charges stemmed from higher labor costs and "supply and demand."

Higher Trucking Charges Solvable

¶10. (U) Most of the debate in Hong Kong, however, has focused on higher trucking charges, since they account for most of the cost differential and policy solutions are clearer.

Mainlandtruckers are not allowed to operate in Hong Kong. All trucks and containers into which goods are loded originate from Hong Kong. Trucking is therefore expensive because of the higher operating costs in Hong Kong. Not only are wages higher, but also parking, insurance, maintenance, and other costs are more expensive. Hong Kong's 8,500 truckers have seen their salaries slashed by over 20 percent since 2001, and trucking companies have replaced fixed salaries with compensation on a per-trip basis. The logistics industry is calling for mainland trucking companies to participate in cross-boundary trucking. While this will accelerate the decline of Hong Kong's trucking industry, it could help maintain business at the port by lowering costs. This strategy could help save the 183,000 jobs both at the port and in ancillary businesses.

¶11. (U) Cross-boundary regulations add to Hong Kong's costs. Currently a trucker has to pay HKD 6,000 (USD 774) per month for a cross-boundary license, ten times more than their counterparts in Guangdong Province. The Guangdong Provincial Government grants these licenses to joint-venture firms between Hong Kong and Chinese companies, which lease them out to truckers. McKinsey estimates license costs represent about HKD 300 (USD 39) per trip.

¶12. (U) A variety of mainland restrictions also prevent Hong Kong,s truckers from usually making more than one trip daily. Until recently, mainland Chinese regulations required that the same trucker, truck, trailer, and empty container stay together for the duration of a journey. Since truckers could not drop off an empty container at a factory and pick up a full one, they had to spend several hours waiting while the factory workers loaded up the empty container. Trucking companies could make two trips a day if they were permitted to drop off empty containers and immediately pick up full ones. If more than one driver could drive the same truck, that truck would also be able to make a second trip on the same day. In January, the mainland lifted its requirement tying containers and trailers to specific trucks, but has not yet issued new regulations. Truckers are afraid to change their practices because of the opacity of the new rules. The mainland also announced that two drivers would be able to drive one truck, but this also has not been implemented.

¶13. (U) Hong Kong truckers face delays not only at the Hong Kong-Shenzhen border, but also at the border between the Shenzhen Special Economic Zone and other mainland

jurisdictions further inland. This "inland Customs" delay often exceeds that at the Hong Kong-Shenzhen border. McKinsey noted that the average trip from Dongguan to Hong Kong is 13 to 15 hours, and truckers spend an average of five to six hours waiting at Customs at the Dongguan-Shenzhen and Shenzhen-Hong Kong border crossings. The HKG is striving to minimize time necessary to cross from Shenzhen into Hong Kong by improving infrastructure, such as constructing the "Western Corridor" bridge from Shekou to Hong Kong, and enhancing efficiency.

¶14. (U) Despite the cost advantage of southern China's ports, Hong Kong retains appeal among shippers, who say that they value the port's easier customs clearance, which involves fewer inspections and more consistent requests for documentation. With 4 to 20 times as many trips to other places in Asia and three times as many to Europe and the United States, Hong Kong also serves more destinations more frequently than do the ports of southern China. Moreover, Hong Kong's status as a duty-free port makes it attractive as a regional warehouse for high-value goods, while its sophisticated legal and financial systems facilitate trade.

Unfortunately for Hong Kong's longer term prospects, the mainland's improving hardware and software are eroding these advantages.

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